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Tax Tips for Construction and Building Contractors

Sales and Use Taxes

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FOREWORD

This publication is designed to help you understand California's Sales and Use Tax Law as it applies to construction and building contractors.

If you cannot find the information you are looking for in this publication, please contact our Information Center at 800-400-7115. Staff will be glad to answer your questions.

For general information about sales and use taxes, your obligations as holder of a seller's permit, and how to file tax returns, see Publication 73, *Your California Seller's Permit*. This publication includes information on obtaining a permit; using a resale certificate; collecting and reporting sales and use taxes; buying, selling, or discontinuing a business; and keeping records. If you do not already have a copy of this publication, you may download one from our website at www.boe.ca.gov or request one from our Information Center.

We welcome your suggestions for improving this or any other tax tip publication. Please send your suggestions to:

Policy Development Section, MIC:50
State Board of Equalization
P.O. Box 942879
Sacramento, CA 94279-0050

Note: This publication summarizes the law and applicable regulations in effect when the publication was written, as noted on the cover. However, changes in the law or in regulations may have occurred since that time. If there is a conflict between the information in this publication and the law, the latter is controlling.

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CONSTRUCTION CONTRACTORS — DEFINITION OF TERMS

CONSTRUCTION CONTRACT — Means and includes a contract, whether on a lump-sum, time and material, cost-plus, or other basis, to:

1. Erect, construct, alter, or repair any building or other structure, project, development, or other improvement on or to real property, or
2. Erect, construct, alter, or repair any fixed works such as waterways and hydroelectric plants, steam and atomic electric generating plants, electrical transmission and distribution lines, telephone and telegraph lines, railroads, highways, airports, sewers and sewage disposal plants and systems, waterworks and water distribution systems, gas transmission and distribution systems, pipelines and other systems for the transmission of petroleum and other liquid or gaseous substances, refineries and chemical plants, or
3. Pave surfaces separately or in connection with any of the above works or projects, or
4. Furnish and install the property becoming a part of a central heating, air-conditioning, or electrical system of a building or other structure, and furnish and install wires, ducts, pipes, vents, and other conduit imbedded in or securely affixed to the land or a structure thereon.

CONSTRUCTION CONTRACTORS — Persons who for themselves, in conjunction with, or by or through others, agree to perform and do perform construction contracts.

UNITED STATES CONSTRUCTION CONTRACTORS — Contractors who for themselves, in conjunction with, or by or through others, agree to perform and do perform construction contracts for the United States Government.

MATERIALS — Means and includes construction materials and components, and other tangible personal property incorporated into, attached to, or affixed to, real property by contractors in the performance of a construction contract and which, when combined with other tangible personal property, loses its identity to become an integral and inseparable part of the real property.

FIXTURES — Means and includes items which are accessory to a building or other structure and do not lose their identity as accessories when installed.

MACHINERY AND EQUIPMENT — Means and includes property intended to be used in the production, manufacturing or processing of tangible personal property, the performance of services or for other purposes (e.g., research, testing, experimentation) not essential to the fixed works, building, or structure itself, but which property incidentally may, on account of its nature, be attached to the realty without losing its identity as a particular piece of machinery or equipment and, if attached, is readily removable without damage to the unit or to the realty.

TIME AND MATERIAL CONTRACT — Means a contract under which the contractor agrees to furnish and install materials or fixtures, or both, and which sets forth separately a charge for the materials or fixtures and a charge for their installation or fabrication.

LUMP-SUM CONTRACT — Means a contract under which the contractor for a stated lump-sum agrees to furnish and install materials or fixtures, or both. A lump-sum contract does not become a time and material contract when the amounts attributable to materials, fixtures, labor, or tax are separately stated in the invoice.

GENERAL APPLICATION OF THE TAX TO INDIVIDUAL BUILDING CONTRACTORS

The operations of building contractors may be considered under three classes of contracts and five operational categories. The classes of contracts are lump-sum, cost-plus, and time and material. The "Liability by Type of Contract" chart on page 3 presents a synopsis of the tax application of the various construction contracts as they apply to United States construction contractors and construction contractors other than United States construction contractors.

The five operational categories are:

1. The contracting for the erection and installation of a building on land.
2. The repair and/or remodeling of existing buildings.
3. The sale of buildings without installation, i.e., packaged prefabricated buildings in "knock down" condition.
4. The erection, installation, and leasing of buildings.
5. The sale and installation of machinery and equipment.

Either the sales or use tax applies with respect to tangible personal property used in the above operations on lump-sum and cost-plus construction contracts as follows:

A. Contract for the erection and installation of buildings on land. (Regulation 1521)

1. As to tangible personal property which is defined as "materials," the tax is due on the cost of such materials to the contractor.
2. As to tangible personal property which is defined as "fixtures," the tax is due on the retail selling price of the fixtures.

B. Property which is used in the repair or remodeling of existing buildings. (Regulation 1521)

Tax applies to the cost of the materials used in remodeling or repair work and the selling price of the fixtures.

C. Sales of packaged prefabricated buildings.

1. The tax applies to the total sales price of small prefabricated buildings, such as a shed or kiosk, which are furnished and installed but **not** physically attached to real property by the seller. When such buildings are required to be physically attached to real property, they are considered to be construction contracts.
2. A contract to furnish and install a prefabricated or modular building similar in size to, but which is not, a relocatable classroom is a construction contract whether the building rests in place by its own weight or is physically attached to realty.
3. Tax applies to 40 percent of the sales price at which "factory-built housing" is sold to a "consumer." This is explained by Regulation 1521.4 which defines "factory-built housing" and "consumer."
4. Manufacturers of factory-built housing who contract to furnish and install the factory-built housing are consumers of materials used and retailers of fixtures furnished. Tax applies as provided in Regulation 1521.
5. Tax applies to 40 percent of the sales price at which a "factory-built school building" is sold to a "consumer." The term "consumer" is defined on page nine of this publication under the heading of "Factory-Built School Buildings."

D. The erection, installation, and "leasing" of buildings.

Where a contract is made for the erection and installation of a building on the customer's land and the payment is received on the basis of an agreed number of "lease" installments, the tax applies to the fixtures and materials in the same manner as a regular construction contract for the erection and installation of a building.

E. Sale and installation of machinery and equipment.

Tax applies to the gross receipts from the sale of machinery and equipment furnished and installed by a construction contractor. If the contract calls only for the furnishing and installation of machinery and equipment, tax applies to the total contract price less those charges excludable from gross receipts under Section 6012 of the Revenue and Taxation Code. As to "machinery and equipment" in United States Government contracts, see subsection entitled "Application of Tax to U.S. Construction Contractors" (page 5).

The chart on the next page presents a synopsis of the tax application of the various construction contracts as they apply to United States construction contractors and construction contractors other than United States construction contractors.

LIABILITY BY TYPE OF CONTRACT

CONTRACTORS IN GENERAL (OTHER THAN UNITED STATES CONTRACTORS)

KIND OF ITEM	HOW ACQUIRED	LUMP-SUM OR COST-PLUS	TIME AND MATERIAL	TIME AND MATERIAL WITH SALES TAX ADDED TO BILLED PRICE OF MATERIALS	UNITED STATES CONSTRUCTION CONTRACTORS
MATERIALS	Purchased ex-tax	Cost	Cost	Billed price	Cost
	Purchased tax-paid	None	None	Excess of billed price over cost	None
	By conversion of realty	None	None	Billed price	None
FIXTURES	Purchased ex-tax	Cost	Billed price	Billed price	Cost
	Purchased tax paid	None	Excess of billed price over cost	Excess of billed price over cost	None
	Manufactured from ex-tax material by installing contractor	Prevailing price to contractors or, if that cannot be established, the amount stated in the price lists, bid sheets or other records, or manufactured cost, including profit, to contractor-manufacturer.	Billed price	Billed price	Cost
	Manufactured from tax-paid material by installing contractor	Excess of prevailing price, or manufactured cost, including profit, over tax-paid cost of materials.	Excess of billed price over tax-paid material cost	Excess of billed price over tax-paid material cost	None

HOW TAX APPLIES TO CONSTRUCTION CONTRACTORS

APPLICATION OF TAX TO CONSTRUCTION CONTRACTORS (OTHER THAN U.S. CONTRACTORS)

A. **MATERIALS** — Contractors are consumers of materials which they furnish and install in the performance of construction contracts, and tax applies to the cost of materials to the construction contractor. However, a construction contractor may contract to sell materials and also to install the materials sold. If the contract explicitly provides for the transfer of title to the materials prior to installation, and separately states the sale price of the materials, exclusive of the installation charge, the contractor will be considered the retailer of the materials.

In the case of a time and material contract, if contractors bill their customers an amount for sales tax computed on their marked-up billing for materials, they are considered to be retailers of materials, and are subject to tax on the amount on which tax reimbursement is charged. If the sale occurs in California, the sales tax applies to the contractors' gross receipts from the sale of the materials. If the sale occurs prior to the time the property is brought into this state, the customer is considered the consumer and must pay their use tax based on the sales price. The contractor must collect this use tax from the customer and pay it to the State of California.

When a contractor fabricates or processes material prior to installation, no tax is due on such processing costs; only the contractor's actual material cost is subject to the tax. Where the contractor sublets fabrication or processing of material to an outside firm, such fabrication is considered part of the taxable cost of materials.

B. **FIXTURES** — Contractors are the retailers of fixtures which they furnish and install, and tax applies to their sales of the fixtures. If the contract states the selling price of the fixture, tax applies to that price. If no sales price is stated, the taxable retail selling price is the cost price of the fixture to the contractor. If contractors purchase a manufactured fixture, the cost price is the sales price of the fixture to them, including any manufacturer's excise tax or import duty imposed prior to the sale by the contractor. However, if the contractor manufactures the fixture, the cost price is considered to be:

1. The prevailing price at which similar fixtures in similar quantities ready for installation are sold by the contractor to other contractors, or
2. If similar fixtures are not sold to other contractors, then the cost price shall be deemed to be the amount stated in the price lists, bid sheets, or other records. If the sale price cannot be established in the above manner, the cost price shall be the aggregate of the following:
 - a. Cost of materials, including freight-in and import duties; direct labor, including fringe benefits and payroll taxes; specific factory costs attributable to the fixture; any manufacturer's excise tax; pro rata share of all overhead attributable to the manufacture of the fixture; and reasonable profit from the manufacturing operations which, in the absence of evidence to the contrary, shall be deemed to be 5 percent of the sum of the preceding factors.
 - b. Jobsite fabrication labor and its prorated share of manufacturing overhead must be included in the sale price of the fixture. Jobsite fabrication labor includes assembly labor performed prior to attachment of a component or a fixture to a structure or other real property.
3. A construction contractor may furnish and install a fixture for a person, other than the owner of the realty, who intends to lease the fixtures in place as tangible personal property and pay tax measured by rental receipts. In this case, the contractor may take a resale certificate from the lessor at the time of the transaction, and the sale to the lessor will be considered a sale for resale.

C. **PREFABRICATED CABINETS** — A cabinet will be considered "prefabricated," and a "fixture" when 90 percent of the total direct cost of labor and material in fabricating and installing the cabinet is incurred prior to affixation to the realty. In determining this 90 percent, the total direct cost of all labor and materials in fabricating the cabinet to the point of installation will be compared to the total direct cost of all labor and materials in completely fabricating and installing the cabinet. Each cabinet will be considered separately if more than one cabinet is fabricated and installed under the contract.

D. **MACHINERY AND EQUIPMENT** — A construction contractor is the retailer of machinery and equipment, even though the machinery and equipment are furnished in connection with a construction contract. If the contract only requires the furnishing and installation of machinery and equipment, tax applies to the total contract price, less installation labor charges and other excludable charges. If a lump-sum contract includes the furnishing and installation of materials, fixtures, and machinery and equipment, tax applies to the price at which such machinery and equipment in similar quantities ready for installation are sold at retail, delivered to the area where the installation takes place. If no such retail price for the machinery and equipment exists, then tax applies to the retail price determined from contracts, price lists, bid sheets, or other records of the contractor.

If the gross receipts cannot be established in the above manner and the machinery and equipment is manufactured by the contractor, the gross receipts from the sale shall be aggregate of the following:

1. Cost of materials, including such items as freight-in and import duties; direct labor, including fringe benefits and payroll taxes; specific factory costs attributable to the machinery or equipment; any manufacturer's excise tax; pro rata share of all overhead attributable to the machinery or equipment, including overhead attributable to manufacturing, selling, contracting, and administration, and; reasonable profit from the manufacture and sale of the machinery or equipment which, in the absence of evidence to the contrary, shall be deemed to be 5 percent of the sum of the preceding factors.
 2. Jobsite fabrication labor and its prorated share of manufacturing overhead must be included in the sale price of the machinery or equipment. Jobsite fabrication labor includes assembly labor performed prior to attachment of a component or the machinery or equipment to a structure or other real property.
- E. **SUPPLIES AND TOOLS FOR SELF-USE** — Contractors are the consumers of supplies such as oxygen, acetylene, gasoline, acid, thread-cutting oil, and tools and parts for tools, which they use in their business, and the tax applies to the sale of such supplies and tools to contractors.
- F. **MISCELLANEOUS** — Items such as adhesives, clips, and nails, could be classified as material, fixtures or equipment, depending on the use made of the product, i.e., if clips are used merely to prevent movement of the item while in production they would be supplies; but if they attach an item to realty, they would be considered materials. However, if attached to a manufactured fixture or piece of equipment, they would assume that identity.
- G. **TAX-PAID PURCHASES RESOLD** — If the contractor sells short ends or pieces which are not used other than in severing them from larger units purchased by him and on which he has paid sales tax reimbursement or use tax, he may claim the deduction for tax-paid purchases resold, but the amount of the deduction shall not exceed the price at which he sells such short ends or pieces.

APPLICATION OF TAX TO U.S. CONSTRUCTION CONTRACTORS

- A. **MATERIALS AND FIXTURES** — U.S. construction contractors are the consumers of materials and fixtures which they furnish and install in the performance of construction contracts with the United States Government. Either the sales tax or the use tax applies with respect to sales of such property to U.S. construction contractors. There is no distinction between the application of tax to materials and fixtures. Only the cost is subject to tax (even though the fixtures are self-manufactured). The sales tax, but not the use tax, applies even though the contractor purchases the property as the agent of the United States.
- B. **MACHINERY AND EQUIPMENT** — U.S. construction contractors are retailers of machinery and equipment furnished in connection with the performance of a construction contract with the United States Government. Tax does not apply to sales of machinery and equipment to U.S. contractors or subcontractors, provided title to the property passes to the United States before the contractor makes any use of it. The contractor may issue a resale certificate. However, if the contractor uses the machinery or equipment before passage of title to the United States, then the contractor is the consumer of the machinery or equipment and either sales tax or use tax applies to the sale to or the use by the contractor of the machinery and equipment.

APPLICATION OF TAX TO RESTAURANT EQUIPMENT CONTRACTORS

The Board of Equalization, in conjunction with the Restaurant Equipment Contractors Association, has made a study of components involved in lump-sum contracts for the furnishing and installing of restaurant equipment.

The following are some items which are usually considered to be materials when furnished and installed by a construction contractor in performing a contract for the food industry:

- Carpeting, including padding and trim when affixed to the real property by glue, nails, etc.
- Doors
- Ducts installed in walls, ceilings, and floors
- Grab bars (for handicapped lavatories)
- Millwork
- Pass window frames and shelves
- Wall corner pieces and wall caps
- Wall covering materials (wallpaper; paneling; etc.)
- Wall flashing
- Wall mirrors

The following items furnished and installed by contractors to the food service industry are generally classified as **fixtures**:

- Bolt-down counter stool bases, with stools attached thereto
- Bolt-down table bases with table tops affixed
- Custom fabricated cash stands
- Custom fabricated cocktail back bar superstructures
- Custom fabricated cocktail back bar
- Custom fabricated cocktail bars
- Custom fabricated counters
- Custom fabricated dishtable assemblies
- Custom fabricated make-up tables
- Custom fabricated pot racks
- Custom fabricated scullery sink assemblies
- Custom fabricated seating assemblies/booth units
- Custom fabricated serving counters
- Custom fabricated service stands
- Custom fabricated soffits
- Custom fabricated walk-in coolers and freezers that are affixed to the real estate, either through a fastening to a building wall or when the walls are imbedded or coved into the building surfaces
- Dispensers for soap, towels, toilet tissue
- Faucets
- Freezers (remote)
- Hoods
- Lighting fixtures
- Motors
- Plumbing fixtures
- Refrigeration compressors
- Refrigerators (remote)
- Safes, imbedded in concrete in the buildings
- Water heaters (built into fixtures or into water systems)
- Water softeners (built into fixtures or into water systems)

Fixtures also include the following items which are built into fixtures or otherwise built into the realty and which may not be removed without damage to the items or the realty:

- Char-broilers
- Dish dispensers
- Dishwashers that are built into a dishtable
- Disposals
- Drink dispensers
- Freezers
- Griddles
- Ice cream cabinets
- Ovens
- Refrigerators

Roll warmer
Scrap chutes
Soda fountain systems
Soup warmers
Syrup rails

The following is a list of items which may be generally considered to be **machinery and equipment** when freestanding or when they are not firmly affixed to the building or built into it or another fixture and which may be readily removed without damage to the building, the unit, or other fixture:

Adding machines
Artifacts items
Bar stools
Beverage and juice dispensers
Bulletin boards
Can openers
Chairs
Char-broilers
Chinaware, silverware, pots and pans, paper goods, culinary items
Coffee makers
File cabinets
Flight-type dishwashers
Floor racks
Griddles
Hot water hoses
Ice bins
Ice cream cabinets
Ice making machinery
Iced tea dispensers
Iced tea machine
Lockers
Microwave ovens (freestanding)
Milk dispensers
Mixers
Ovens
Portable bins and tables
Ranges
Reach-in freezers (self-contained)
Reach-in refrigerators (self-contained)
Roll covers
Safes
Salamanders
Scales
Shelving units
Silverware boxes
Slicers
Table lamps
Tables
Time car racks
Time clocks
Toasters

SUBCONTRACTORS

A subcontractor who has furnished and installed materials or fixtures for a prime contractor must pay tax on the cost of the materials or in the case of non U.S. contractors the retail selling price of the fixtures installed. **A subcontractor may not accept a resale certificate from a prime contractor for materials the subcontractor furnishes and installs.** Under most circumstances, subcontractors may also not accept a resale certificate from a prime contractor for fixtures the subcontractor furnishes and installs. However, a subcontractor may furnish and install a fixture for a person, other than the owner of the realty, who intends to lease the fixture in place as tangible personal property and pay tax on the rental receipts. In this latter case, the subcontractor may accept a resale certificate from the lessor at the time of the transaction.

FACTORY-BUILT HOUSING

Tax applies to 40 percent of the sales price at which factory-built housing is sold to a consumer. A consumer is any person purchasing factory-built housing for use in erecting or remodeling a building on land used for a residential dwellings or as an institution for resident or patient care. A retailer who makes retail sales of "factory-built housing" claimed to be subject to tax measured by 40 percent of the purchase price must obtain from the consumer a signed "60 percent exclusion certificate." See Regulation 1521.4.

When manufacturers of factory-built housing contract to furnish and install the factory-built housing manufactured by them, they are considered the consumers of the materials used in building and installing the factory-built housing and the retailers of the fixtures. Tax applies in accordance with Regulation 1521 rather than Regulation 1521.4.

FACTORY-BUILT SCHOOL BUILDINGS

A contract to furnish and install a factory-built school building (FBSB) is not a construction contract, but rather is a sale of tangible personal property. **For purposes of local tax allocation, the place of sale of an FBSB is the place of business of the retailer, not the jobsite location.**

In general, a FBSB is defined as any building which is designed or intended for use as a school building and is wholly or substantially manufactured at an offsite location for the purpose of being assembled, erected or installed on a site owned or leased by a school district or a community college district. Buildings that are licensed by either the Department of Motor Vehicles or the Department of Housing and Community Development are not FBSBs.

Tax applies to 40 percent of the sales price at which the FBSB is sold to a consumer, excluding on-site installation labor. The following are examples of persons defined as consumers:

1. A school district or a community college district, or
2. A contractor who purchases a FBSB for the purpose of fulfilling the requirements of an existing contract with a school district or a community college district to furnish and install such a building

For more detailed information on FBSBs, please refer to Regulation 1521.

MANUFACTURED HOUSING/MOBILEHOMES

The application of tax to transactions involving mobilehomes and related accessory items or improvements or additions to realty is covered in Publication No. 47, "Tax Tips for Manufactured Mobilehomes and Factory-Built Housing," which is available from our Information Center.

ELECTRIC SIGNS

Beginning October 1, 2000, contractors who furnish and install on-premise electric signs for a single (lump-sum) contract price should report tax on 33% of the total contract price. Total contract price includes all charges for materials, fabrication labor, installation labor, overhead, profit, and any other charges associated with the sale and installation of the sign.

For example, on October 1, 2000, you contract with a customer to furnish and install an electric monument sign for a lump-sum contract price of \$20,000. Under the new rules, you are required to report tax on \$6,600 ($33\% \times \$20,000 = \$6,600$). You would report tax using the tax rate in effect at the location where the sign is installed. It is presumed that the remaining \$13,400 ($\$20,000 - \$6,600 = \$13,400$) is for nontaxable installation labor.

Please note: This reporting method is available only on the sale and installation of an electric sign. You may not use it to report the sale of a nonelectric sign. This change does not affect your responsibility to report tax on the selling price of a sign when you sell a sign without installing it, or when you separately state the selling price of a sign you install.

Example 1: You sell a sign for \$15,000 to a customer who has hired another contractor to install it. You must report tax on \$15,000 at the tax rate in effect at the sales location.

Example 2: You contract to furnish and install an electric sign for which you separately state a sale price of \$15,000 for the sign and \$5,000 for installation labor. Because you have separately stated the selling price, you must report tax on \$15,000, using the tax rate in effect at the location where the sign is installed.

Remember, charges for installation labor are nontaxable. For example, when you install a sign sold by someone else or owned by the person for whom you are doing the installation, all your labor charges are nontaxable. However, if you furnish and install a sign with separately stated charges for the sign and the installation labor, you may be required to document that the charges for installation do not include taxable fabrication labor. For example, you furnish and install a sign and separately state labor charges of \$12,000. You may be required to provide bid sheets or time sheets that document the entire \$12,000 was for installation labor and not fabrication of the sign.

MODULAR FURNITURE

Effective December 1, 1999, Regulation 1583, "Modular Systems Furniture," provides guidelines for sales of modular systems furniture. The regulation specifically states that a contract to sell and install modular systems furniture is a contract for the retail sale of the tangible personal property and not a construction contract. This is true whether or not the systems are affixed to realty. For contracts to sell and install modular systems entered into on or after October 1, 1999, the regulation allows persons selling and installing the modular systems to claim 10 percent of the total contract price, excluding charges attributable to free-standing furniture, as the charge for nontaxable installation labor.

If you are a subcontractor and have contracted with the seller to assemble and install a modular system (the system components being provided by a prime contractor or others) or if you are reconfiguring an existing system, the allowable 10% deduction does not apply to your contracts. You should continue to report and separately account for your taxable and nontaxable labor charges. For more information regarding sales of modular furniture, please call our Information Center.

CONSTRUCTION CONTRACTORS— USE OF RESALE CERTIFICATES

Under Regulation 1521, construction contractors are generally considered the consumer of materials which they furnish and install in the performance of a construction contract to improve real property. However, if the contract (other than a U.S. government contract) explicitly provides for transfer of title to the materials prior to installation, and the sales price of the materials is separately stated in the contract, the contractor will be deemed to be selling the materials. In addition, if a contractor bills their customer an amount for "sales tax" computed upon a marked up billing for materials under a time and material contract, it will be assumed that he or she is selling the materials.

When construction contractors sell materials which they install, the sale of the materials is a retail sale. Consequently, there are no circumstances under which a construction contractor may accept a resale certificate from a prime contractor, interior decorator, department store, or others for materials which he furnishes and installs.

In general, construction contractors (other than U.S. construction contractors) are the retailers of fixtures which they furnish and install. However, in some instances a construction contractor may furnish and install a fixture for a person, other than the owner or lessor of the realty, who intends to lease the fixture in place as tangible personal property and pay tax measured by rental receipts. In this case the contractor may take a resale certificate from the lessor at the time of the transaction, and the sale to the lessor will be considered a sale for resale. Under no other circumstances may construction contractors accept resale certificates for fixtures which they furnish and install.

EXCESS TAX REIMBURSEMENT

Since a contractor is the consumer of materials furnished and installed in the performance of a lump-sum construction contract, tax reimbursement collected on the total contract price constitutes excess tax reimbursement. Such excess tax reimbursement must be returned to the customer or paid to the state. However, off sets will be allowed, as explained in Regulation 1700, "Reimbursement for Sales Tax," against any tax liability of the contractor on the same transaction.

MATERIALS AND FIXTURES USED OUTSIDE OF CALIFORNIA

Where contractors have a contract to improve real property outside of California, their use of materials and their sales of fixtures are not subject to the tax provided they fulfill certain conditions. The sales of fixtures, which occur upon installation, are sales outside this State and tax does not apply thereto by virtue of the fact that title passes at the out-of-state point. The purchases of the materials in California are not subject to the tax under the conditions specified in Section 6386 of the Revenue and Taxation Code. Those conditions are, that purchasers hold a valid seller's permit, that they incorporate the property into real property located outside this State, and that they certify in writing to the seller at the time of purchase, that the property will be used in the specified manner. **A certificate provided by the contractor to the seller subsequent to the time of purchase will not be recognized.** As to fixtures, the contractor may either provide the exemption certificate described above or issue a valid resale certificate to the seller.

INTERSTATE AND FOREIGN COMMERCE

Sales of buildings without installation or erection are exempt from the tax **when the contract of sale provides that the seller shall deliver the buildings to the purchaser at an out-of-state point.** This condition of the contract may be fulfilled by shipping the building to a point outside the state by means of (1) facilities which are operated by the retailer, (2) delivery by the retailer to a carrier for shipment to a consignee at such point, or (3) delivery by the retailer to a custom's broker or forwarding agent for shipment outside this State. Sales of buildings or other tangible personal property are also exempt if they are sold to foreign purchasers for shipment abroad and delivered to a conveyance furnished by the purchaser for the purpose of carrying and taking the property abroad. Proof must be retained that the property was carried to the foreign destination.

TRANSPORTATION CHARGES

In making purchases subject to tax, the freight charges by the seller to the contractor may or may not be subject to tax, depending upon the conditions of the sale. The same principles that apply to freight charges on the purchase of tangible personal property also apply to the sale of tangible personal property by the contractor. For example, where a sale is made of a prefabricated building without erection or installation, no tax will apply to separately stated freight charges made for the shipment of the building by independent contract or common carrier. Where tangible personal property is shipped by the seller's own truck or facility, separately stated charges for such delivery are subject to tax unless the sales agreement specifically provides that title to the goods passes at the seller's place of business.

Construction contractors who bill their customers for sales tax on materials used on time and material contracts are "retailers" of the materials. Quite often, contractors will deliver materials to jobsites by use of their own transportation facilities and make a separate charge to the customers for such delivery. Normally, unless otherwise stipulated by contract, title to the materials passes at time of delivery to the jobsite. Under such circumstances, the sales of materials and such separately stated delivery charges are subject to sales tax. However, separately stated delivery charges may be exempt from the tax if title to the materials explicitly passes to the customer prior to delivery.

For further information on transportation charges, refer to Regulation 1628, "Transportation Charges."

BAD DEBTS

When contractors are the consumers of materials (or fixtures in U.S. Government contracts) which they furnish and install, there is no basis for claiming bad debts. In cases where they are the sellers, bad debts losses incurred are to be treated in the same manner as those resulting from other types of retail sales.

Sellers may claim a deduction for bad debts found to be uncollectable and charged off for income tax purposes. Should the uncollectable amounts include exempt items, such as installation labor or interest charges, as well as taxable items, a bad debt deduction may be claimed only in respect to the unpaid amount upon which the tax has been paid. In determining this amount, all payments and credits to the accounts must be apportioned to the taxable and nontaxable elements which make up the amount the purchasers agreed to pay.

If any accounts found worthless and charged off for income tax purposes are subsequently collected in full or in part, the amount collected must be included in the first return filed after receiving the funds.

- No deduction is allowable for expenses you may incur in attempting to collect the bad account.
- No deduction is allowable for that portion of debt recovered and retained by or paid to a third party as compensation for collecting the account.

See Regulation 1642, "Bad Debts" for more information.

LOCAL SALES AND USE TAXES

All of the provisions of the State Sales and Use Tax Law and regulations adopted thereunder relating to construction contractors, other than those relating to the rate of tax, are applicable to the state-administered local sales and use taxes.

The jobsite is regarded as a place of business of a construction contractor or subcontractor. It is here that the sales of the fixtures and the use of the materials occur.

Effective January 1, 1995, construction contractors may elect to allocate the local sales and use tax derived from construction contracts of \$5,000,000 or more directly to the local jurisdiction where the jobsite is located. This qualifying contract price applies to each contract or subcontract for work performed at the jobsite, and not to the total value of the prime contract.

The allocation is accomplished by obtaining a sub-permit of your seller's permit for a specific jobsite. For information about the conditions to obtain the sub-permit, please contact our Information Center.

DISTRICT TAXES

All of the provisions of the State Sales and Use Tax Law and regulations adopted thereunder relating to construction contractors, other than those relating to the rate of tax, are applicable to state-administered transactions (sales) and use taxes imposed by special taxing districts.

The jobsite is regarded as a place of business of a construction contractor or subcontractor and is the place of sale of "fixtures" furnished and installed by contractors or subcontractors. The place of use of "materials" is the jobsite.

Accordingly, if the jobsite is in a district having state-administered transactions (sales) and use taxes, the transaction (sales) tax applies to the sale of fixtures, and the use tax applies to the use of materials unless purchased in a district having state-administered transactions (sales) and use taxes and not purchased under a resale certificate. If the jobsite is in a district without a state-administered tax, state-administered transactions (sales) tax will not apply to the sale of the fixtures even though the contractor's principal place of business is in a district with such a tax.

If fixtures are purchased by a contractor tax paid in a district having state-administered transactions (sales) and use taxes, the contractor, upon installing the fixtures at a place without such a tax, is entitled to a credit for the tax of the district of purchase.

Unless "materials" are purchased under a resale certificate, the district tax applies to "materials" purchased and delivered within a special taxing district even though such "materials" may be used outside the district. The district tax does not apply to property purchased from a retailer within the district for use outside the district and which is shipped to a point outside the district pursuant to the contract of sale, by delivery to such point by the retailer or his agent, or by delivery by the retailer to a carrier for shipment to a consignee at such point.

As construction contractors are retailers of fixtures which they furnish and install in fulfilling contracts other than construction contracts with the United States, the district tax applies to "fixtures" furnished and installed by construction contractors on or after the operative date of the district transactions (sales) and use taxes ordinance unless a fixed price construction contract was entered into prior to the operative date of the ordinance. The district tax applies to "materials" purchased by a construction contractor on or after the operative date of the ordinance unless a fixed price contract for the purchase was entered into with the contractor's supplier prior to the operative date of the ordinance.

Contractors performing construction contracts for the United States are consumers of both “materials” and “fixtures.” Tax applies to “fixtures” in the same manner as it does to “materials” furnished and installed by such contractors. Under such contracts the place of use of materials and fixtures is the jobsite. Accordingly, if the jobsite is in a district having state-administered transactions (sales) and use taxes, the use tax applies to the use of the materials and fixtures unless purchased in a district having state-administered transactions (sales) and use taxes and not purchased under a resale certificate. The district tax applies to both “materials” and “fixtures” purchased by a construction contractor for use in fulfilling contracts with the United States on or after the operative date of the transactions (sales) and use taxes ordinance, unless a fixed price contract for the purchase was entered into with the contractor’s supplier prior to the operative date of the ordinance.

PROCEDURES FOR ASCERTAINING TAX LIABILITY

METHOD OF PURCHASING

Contractors’ operations may require that they pay tax on some of their purchases of tangible personal property as a consumer and to purchase other tangible personal property for resale and pay tax upon the selling price to their customers. This raises the question of the most efficient method of purchasing. Usually contractors will find it easier to set up their purchasing on the basis of the preponderance of the type of operation that they conduct. If most of their tax liability is in connection with their own self-consumption, they may prefer to purchase everything on a tax-paid basis and when they make a sale of property take a tax-paid purchases resold deduction under Regulation 1701, “Tax-Paid Purchases Resold”. On the other hand, if most of their sales represent sales of tangible personal property without erection and installation, and if they cannot ascertain at the time of purchase whether particular property will be resold or used they may prefer to purchase the property on an ex-tax basis and report tax on items which they consume and do not resale. Contractors with complex operations will often wish to purchase on the basis of the type of commodity, in which case they will prefer to purchase some items on a tax-paid basis and others on an ex-tax basis. Whatever method is used, great care must be exercised in recording their purchasing data and ascertaining their tax liability.

Where merchandise is purchased on a tax-paid basis, contractors should be careful to see that the following points, among others, are covered:

- A. Has their vendor charged tax on freight which might, under the provisions of Regulation 1628 not be subject to the tax?
- B. Has the proper deduction been taken of the tax-paid cost of materials going into prefabricated buildings upon which a tax was paid on the selling price (or was sold in interstate and foreign commerce)?
- C. Has any tax been paid to the vendor on any items of machinery and equipment upon which tax was paid on the selling price?
- D. Have proper certificates been filed with the vendors in connection with materials and fixtures used or sold at an out-of-state point? (See “Materials and Fixtures Used Outside of California,” page 10.) When making purchases for this purpose, the claim for exemption must be made at the time of purchase.

Where construction contractors are purchasing on an ex-tax basis, their liability must be ascertained by determination of materials used or fixtures sold. In the case of materials purchased under valid resale certificates, liability for tax arises when the materials are committed to the fulfillment of a construction contract. The withdrawal from storage for transportation to the site where the property will be used in construction operations constitutes such a commitment. The tax must be paid with the return for the period in which the commitment took place. It is not permissible under the law to wait until the job is completed before reporting and paying tax upon the purchase price. In the case of materials purchased ex-tax from out-of-state vendors for use (not resale) in California, the liability for tax arises when the materials enter California. In the case of fixtures, liability for the tax arises when the fixture is installed, as this is when the sale of the fixture takes place.

Great care must be exercised in the assembling of the data and the preparation of the return. Some of the points to be covered are:

- A. All purchases must be controlled and analyzed for tax status. Contractors’ records should be maintained in such a manner that they will be certain that they have paid tax in the case of lump-sum and cost-plus construction contracts on the tangible personal property used in the fulfillment of the contract, keeping in mind that if they manufacture their own fixtures, their tax liability will be on the basis explained in the section entitled “How Tax Applies to Construction Contractors (see page 4).”
- B. Taxpayers must determine the points in their accounting and office procedures at which they will best be able to ascertain their tax liability.

C. Duplication of “control points” must be eliminated to avoid duplicate reporting of the tax.

- 1 . Purchases subject to use tax made from vendors not having certificates from the taxpayer will be accumulated from their purchasing or cost records.
 2. Withdrawals from “ex-tax” inventory for contractor’s own use would probably be controlled from requisition slips.
- These are merely given as examples. Contractors will of course develop their own “control points” to fit the procedures best suited to their particular operations.

If any questions which may not be covered in this publication arise, please contact the Board’s Information Center for assistance.

“FIXED-PRICE” CONTRACT EXEMPTION

A. Transactions (Sales) and Use Tax

The ordinances imposing the transactions (sales) and use tax contain provisions which state that the tax does not apply to the gross receipts from the sales or purchases of tangible personal property in the district, if the seller is obligated to furnish and the buyer is obligated to purchase the property for a **fixed price** pursuant to a contract **entered into prior to the operative date of the ordinance**.

This exemption applies only to the contract between you, as the contractor, and your customer. You, as a construction contractor may not file an exemption certificate with your suppliers for the purpose of obtaining a refund of new transactions taxes enacted during the period of a contract. You must be a party to a fixed-price contract directly with your supplier.

B. “Fixed-Price” Contract Defined

A “fixed-price contract” is a contract that obligates both the buyer and seller to the specified terms. The buyer must be obligated to purchase and the seller must be obligated to sell, a determinable quantity of tangible personal property identified by the contract. In addition, if either party has the right to terminate the contract, conditioned only upon notice, whether or not such right is exercised, it is not a “fixed-price contract.” Also, if the contract is contingent on the occurrence of an act or an event, it is not a “fixed-price contract.”

“Fixed-price” means that the contract price cannot be increased for any reason. In addition, the tax amount or rate must be specifically stated in the contract.

A contract for a “fixed-price” includes:

- (A) A unit price contract under which each unit price is affixed dollar amount which may not be increased or decreased by reason of any changes in tax rates, cost of materials, and so forth.
- (B) A guaranteed maximum contract under which the guaranteed maximum amount cannot be increased by reason of changes in tax rates, cost of materials, and so forth.

FOR MORE INFORMATION

FOR MORE INFORMATION

If you have a general tax question or would like to order a publication, please call our Information Center and talk to a customer service representative. Representatives are available from 8:00 A.M. to 5:00 P.M., Monday-Friday, excluding State holidays. Please call:

800-400-7115

For TDD assistance (telephone device for the deaf), please call:

From TDD phones:
800-735-2929

From voice phones:
800-735-2922

FOR QUESTIONS REGARDING YOUR ACCOUNT

If you have a question regarding your account (for example, a question about an audit, a tax payment, or a billing), please call the office that maintains your records. Their telephone number is printed on your tax return. Or see page 15 for a list of local Board office telephone numbers.

TO VERIFY A SELLER'S PERMIT NUMBER

If another seller has given you a resale certificate to make a purchase for resale, you can contact us to verify the seller's permit number provided by that seller. You can call toll-free, 888-225-5263, or you can visit our website at www.boe.ca.gov. Both services are available seven days a week. You should also have available the name of the business, the business address, and the name of the business owner, to compare with the information we provide.

FAX-BACK SERVICE

Selected forms and notices are available on our automated fax-back service. Call 800-400-7115 at any time and choose the fax option.

HELPFUL PUBLICATIONS AND REGULATIONS

How You Can Obtain a Publication or Regulation

Call our Information Center. A customer service representative will help you during working hours. If you know the name of the publication, form, or regulation you need, you can call outside of working hours and leave a recorded message. Certain documents are also available on our fax-back service, described above.

Send a fax request. You can request fax copies of selected forms and publications. Call 800-400-7115 and choose the fax option.

Use the Internet. Certain regulations and publications are available on our Internet home page. See page 15.

Regulations. The following regulations may be of interest to you:

- 1521 "Construction Contractors"
- 1521.4 "Factory-Built Housing"
- 1628 "Transportation Charges"
- 1700 "Reimbursement for Sales Tax"
- 1701 "Tax-Paid Purchases Resold"
- 1806 "Construction Contractors — Tax Application Under Bradley-Burns Local Sales and Use Tax"
- 1826 "Construction Contractors — Tax Application Under Transactions (Sales) and Use Tax"

Publications. You may find the following publications to be helpful. The letter C, F, K, S, or V following a publication indicates the publication is available in Chinese, Farsi, Korean, Spanish, or Vietnamese:

- 17 Appeals
- 44 District Taxes
- 51 Guide to Board of Equalization Services (C, K, S, V)
- 70 The California Taxpayers' Bill of Rights (C, K, S, V)
- 73 Your California Seller's Permit (C, K, S, V)
- 74 Closing Out Your Seller's Permit (S)
- 75 Interest and Penalty Payments (C, K, S, V)
- 76 Audits (F, K, S)

TAX INFORMATION BULLETIN

As a registered seller, you will receive a copy of the *Tax Information Bulletin* with your returns. The *Bulletin* includes articles on the application of law to specific types of transactions, announcements regarding new and revised publications, and other articles of interest to sellers. If you file only one return a year, you will receive only one bulletin. If you would like to receive all four bulletins, please write to the following address and ask to be added to Mailing List #15: State Board of Equalization; Mail Services Unit, MIC:12; Attn: Addressing Systems; P.O. Box 942879; Sacramento, CA 94279-0012. Tax Information Bulletins may also be downloaded from our website.

WRITTEN TAX ADVICE

For your protection, it is best to get tax advice in writing. If you write to the Board for advice regarding the taxability of a transaction and the Board's written reply is incorrect, you may be relieved of tax, penalty, or interest charges. For this relief to apply, a request for advice must be in writing, identify the taxpayer to whom the advice applies, and fully describe the facts and circumstances of the transaction. You should send your request to the Board office that handles your account.

INTERNET — WWW.BOE.CA.GOV

We maintain a variety of information on our website, including selected publications and regulations, sales and use tax rates by county, Board field office addresses and telephone numbers, Taxpayers' Bill of Rights Hearings, publications order forms, an agency profile, and Board Member biographies.

CLASSES

You can enroll in a basic sales and use tax class offered by some local Board offices. You should call ahead to find out whether a class is offered for beginning sellers.

TAX EVASION HOTLINE

Tax evasion hurts businesses that are paying their fair share. If you wish to report a case of suspected tax evasion, call our toll-free hotline at 888-334-3300. Please call during working hours.

BOARD FIELD OFFICES

CITY	AREA CODE	NUMBER	CITY	AREA CODE	NUMBER	CITY	AREA CODE	NUMBER
Bakersfield	661	395-2880	Riverside	909	680-6400	Torrance	310	516-4300
Culver City	310	342-1000	Sacramento	916	227-6700	Van Nuys	818	904-2300
El Centro	760	352-3431	Salinas	831	443-3003	Ventura	805	677-2700
Eureka	707	445-6500	San Diego	619	525-4526	West Covina	626	480-7200
Fresno	559	248-4219	San Francisco	415	356-6600	Offices for Out-of-State Accounts		
Kearny Mesa	858	636-3191	San Jose	408	277-1231	Chicago, IL	312	201-5300
Laguna Hills	949	461-5711	San Marcos	760	510-5850	Houston, TX	281	531-3450
Norwalk	562	466-1694	Santa Ana	714	558-4059	New York, NY	212	697-4680
Oakland	510	622-4100	Santa Rosa	707	576-2100	Sacramento, CA	916	227-6600
Rancho Mirage	760	346-8096	Stockton	209	948-7720			
Redding	530	224-4729	Suisun City	707	428-2041			

TAXPAYERS' RIGHTS ADVOCATE

The State Board of Equalization wants to make dealing with us as easy as possible. Consequently, we have appointed a Taxpayers' Rights Advocate to help you with problems you cannot resolve at other levels.

Taxpayers' Rights Advocate
State Board of Equalization
450 N Street, MIC:70
PO Box 942879
Sacramento, CA 94279-0070

Telephone: 916-324-2798 or 888-324-2798
Fax: 916-323-3319

To request a copy of Publication 70, *The California Taxpayers' Bill of Rights*, please call the Information Center, 800-400-7115.